> study area, consistent with Section 254(e), the CLEC cannot 'creamskim' or serve only low cost areas[42]

is simply wrong because of the availability of resale or "rebundled" elements. Further, there is no requirement that the CLEC may price its resold services in the high cost area at a price which will not "win" it any business, and if it has no business, it will have no expense.

A new competitor enters a rural service area only if it believes it can make a profit. Profit is made only where revenues exceed the cost of service. Logically only the most profitable low-cost, high-volume customers will be targeted by a competitor for investment in facilities. This is competition. This is capitalism. No CLEC salesman is going to drive for miles and miles, through creeks and dirt roads, in order to sign up a customer that loses his company money. Such a scenario is irrational. Whether a CLEC has to advertise or not, the truth of the matter, consistent with the aggressive principles of competition, is that the most lucrative customers will receive the attention of a competitor.

CLEC attention to the most lucrative low-cost, high-volume customers will be increased by the windfall of averaged support they will receive by targeting and capturing these customers. As if these customers were not attractive enough, the recommended support mechanism will exacerbate the situation. CLECs will be able to calculate the extra averaged support they will receive, in excess of their actual costs, and use this difference to unfairly undercut the ILECs prices. In addition, the recommended support mechanism will encourage overbuilding in low-cost areas since it will overcompensate the builders through its use of averaged support. In essence, a CLEC will be able to double-dip by reselling remote facilities for less than the actual cost to maintain them, and then

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42 *Recommended Decision* at para. 297.

creamskim support in the towns. The grant of study area averaged support to carriers without facilities covering the same area and without the same embedded cost will send contorted economic incentives to potential competitors and is antithetical to competitive neutrality.

If it really believes in the principle of competitive neutrality, the Commission will flow high cost support only to the provider who maintains the facilities and at its costs. If a CLEC is reselling a loop based upon a rate that includes universal service support, the CLEC should not get the high cost support for that loop since the loop is already receiving the support because the price it is charged for resale is based on a supported retail price. The law requires that support shall be used "only for the provision, maintenance, and upgrading of facilities."[43]

RTC members have spent decades attempting to build their towns and outlying areas into viable communities. A historical commitment to universal service by rural telephone companies, Congress, and the FCC has made this possible. Ironically, the profitability of these once-ignored areas is attracting competitors. RTC members have no problem with competition, but true competition based on the marketplace cannot develop where one side receives support based on the incumbents' costs. The Joint Board's portable support recommendation sends perverse economic signals that could devastate the higher ideal of universal service. If dual goals of competition and universal service are to be balanced, it will take an accurate, sufficient, and delicately disaggregated support mechanism, not a clumsy and averaged one, to achieve a desirable balance between competition and universal service.

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[43] 47 U.S.C. Section 254(e).

g. SUPPORT FOR MULTILINE BUSINESS, SECOND LINES AND SECOND HOMES CANNOT LAWFULLY OR PRACTICALLY BE EXCLUDED, AND THERE ARE SOUND PUBLIC POLICY REASONS TO INCLUDE THEM.

Adoption of the Joint Board's recommendation to provide support only to single-connection businesses would deal a harmful blow to rural development and universal service, and violate the 1996 Act. This decision discriminates against small businesses who will not benefit from the discount offers that large, high-volume businesses receive. Most important, the *Recommended Decision* is contrary to the Act's mandate that subscribers in rural areas "should have access to telecommunications and information services, including interexchange services and advanced telecommunications and information services, that are reasonably comparable to those services provided in urban areas and that are available at rates that are reasonably comparable to rates charged for similar services in urban areas."[44]

In fact, the Joint Board belies its own logic behind the decision when it states "that small businesses lack the ability to use alternatives to the public switched network that are available to large corporations."[45] If this is true, a double-connection business is out of luck when it comes to universal service support. The small businessman, with a single telephone line and an additional computer or fax line, has the choice to either drop one of his essential lines or move out of the rural area if he wants to have a phone bill at a rate that is "reasonably comparable to rates charged for similar services in urban areas."[46] Moving to where business rates are reasonable is not a universal service principle.

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[44] 47 U.S.C. Section 254(b)(3).

[45] *Recommended Decision* at para. 91.

[46] 47 U.S.C. Section 254(b)(3).

The Joint Board's *Recommended Decision* will lead to burdensome business rates in rural areas for the small businessman, possibly deterring businesses from locating in rural regions. For years, rural America had experienced a depressing wave of "outmigration" as people left remote regions in search of employment. In the last few years, through the use of telecommunications, rural telephone companies have attracted businesses to their towns, reversing the outmigration trend and creating jobs.[47] The *Recommended Decision* to support only single-line businesses could wreak havoc on fragile rural economies.

Single-connection local business support, in addition to unfairly squeezing the small businessman and the rural economy, is squarely at odds with the Act. Congress was well aware of the differences between business and residence lines, and the Conference Committee chose not to limit toll rate averaging clause to residential service.[48] Discriminating against small rural businesses is not only unfair, it violates the intent of the Act.

Once again, with its decision to provide support only "to those services carried on a single connection to a subscriber's principal residence,"[49] the Joint Board ignores the urban/rural comparability mandate of the Act. Additionally, the Act mandates "access to advanced services"[50]

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47 Bill Richards, "Linking Up: Many Rural Regions Are Growing Again." *The Wall Street Journal*, November 21, 1994, p. A1.

48 Congress rejected language proposed by AT&T which would have limited the toll rate averaging to residential service. The conference report text suggests that Congress did not intend to limit Section 254(g) to residential services. *See, Joint Explanatory Statement of the Committee of Conference* at 129 and 132.

49 *Recommended Decision* at para. 89.

50 47 U.S.C. Section 254(b)(2).

and "just, reasonable, and affordable rates."[51] Without any universal service support for a second residential line, a rural resident will not have comparable service or rates compared to urban residents as to access to advanced services such as Internet. Certainly, this is not comparable to the options that an urban resident has.

Not only does the primary line support recommendation ignore the clear urban/rural comparability mandate of the Act, but, as a practical matter, it will be nearly impossible to administer and bill such a scenario. For example, some residences have more than one family, each with its own line. Apartment classification will be tricky. A residence might have one CLEC line and one ILEC line, or perhaps one wireline and one wireless. Multiple lines in a single residence could be under multiple names and even multiple providers. It could take an effort as complex and expensive as the national Census, including surveys and door-to-door visits, to sort through the myriad of different residential line support permutations. Such a Byzantine system would fail any cost/benefit analysis.

The Joint Board concludes "[t]here is no evidence that the additional cost of supporting second or vacation residences is justified in light of the presumption that owners of these residences can afford to pay rates that accurately reflect the carrier's costs."[52] This *Recommended Decision* illegally introduces means testing into the high cost support mechanism. The Act emphatically mandates high cost support for "all regions of the Nation"[53] and ensures access to "[c]onsumers in all regions of the nation, including low-income consumers and those in rural, insular, and high cost

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[51] 47 U.S.C. Section 254(b)(1).

[52] *Recommended Decision* at para. 90.

[53] 47 U.S.C. Section 254(b)(2).

areas."[54] Nowhere does the Act exclude second residences, vacation homes, or consumers who have worked hard and saved money.

The suggestion to exclude second homes from high cost support is a remnant from the old CC Docket 80-286, which Congress rejected. Chairman Reed Hundt, in a recent speech, stated that the recommendation to exclude support to "vacation homes and ski chalets... is a major step forward to reduce total subsidies."[55] The Joint Board does not state the basis for its presumption, but clearly not every second residence is a luxury investment of yuppies and movie stars; some are maintained by working class people whose living requires them to make seasonal moves or to live apart from their families. There is no practical way to distinguish between the access line to a ranch house and the phone in the trailer of the stablehand whose family has to remain near schools or a spouse's job. Even if the ranch owner can afford to pay the full cost for a connection to his second home, it is not the proper role a carrier or the FCC to pry into the income level of every subscriber. This proposal is a manifest violation of the Act's intent to provide all consumers and all regions of the country "access to advanced telecommunications and information services"[56] and to ensure urban/rural comparability.

Additionally, the exceedingly complex and intricate mechanism needed to determine each subscriber's number of homes, and possible extenuating circumstances would fail any cost/benefit analysis. It will be nearly impossible for US West in Colorado to determine whether one of its customers in a ski chalet happens to have an apartment in the Washington, D.C. Bell

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[54] 47 U.S.C. Section 254(b)(3).

[55] Reed Hundt, NARUC, San Francisco, November 28, 1996.

[56] 47 U.S.C. Section 254(b)(3).

Atlantic territory. No mechanism will be able to determine if a second residence is actually rented to another, possibly low-income, family. Such a mechanism would require the phone company to determine whether the billed party owns the billed residence, and if so, whether they or a possible spouse owns any other residences throughout the entire United States. The introduction of means testing into the high cost support mechanism is at odds with the Act, raises a host of privacy concerns, and would be a logistical and administrative horror.

B. COMPETITIVE BIDDING IS CLEARLY IN CONFLICT WITH THE ACT.

The Joint Board refuses to give the competitive bidding idea the proper burial it deserves. Even though the Joint Board does "not adopt any specific competitive bidding plan at this time,"[57] it plans to "continue to explore the possibility."[58] Competitive bidding is in conflict with the Act. The authority to designate eligible carriers is given to the state commissions,[59] which in turn must be guided by the principles and goals set forth in Section 254. The Commission clearly does not have the authority to compel states to proceed by competitive bidding.

Even if the Commission had such authority or works with the states to compel all state designated eligible telecommunications carriers to bid, the bidding process would not produce the quality of service contemplated by the Act, since the winning bidder could be the carrier which intends to commit the least amount of resources to the area. Competitive bidding is a "race to the bottom" and at odds with the Act's emphasis on "quality services."[60] The superficial conjecture that

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57 *Recommended Decision* at para. 341.

58 *Ibid.*

59 47 U.S.C. Section 214(e).

60 47 U.S.C. Section 254(b)(1).

bidding for support would force carriers to find ways to provide service in a more cost effective manner is not practical in the real world, at least absent an administratively unwieldy regulatory review of construction plans on an initial and continuing basis. Also, basing the study area support level on the lowest bid from all eligible carriers[61] would risk providing a support level that is neither "sufficient" nor "predictable." Such a scenario could lead to a drastic shortfall in the amount of high cost support necessary to maintain universal service. Basing all support on the lowest bid is at odds with the principle of competitive neutrality, since it would allow the competitive low bidder to target the customers it believes it can support with its low bid, while leaving the ILEC with inadequate support for the remaining high cost customers.

Additionally, the circumstances that allowed a state to designate a carrier as an eligible telecommunications carrier might change after competitive bidding. An auction changes the circumstances in which the state chooses, in the public interest and in accordance with Section 214(e), an additional eligible telecommunications carrier. After a "race to the bottom" bid, it may no longer be in the public interest for the state to have chosen the additional eligible carrier. The folly of competitive bidding should be abandoned.

C. THE BENCHMARK PROPOSAL DOES NOT REASONABLY MEASURE WHAT A RURAL LEC SHOULD RECOVER BEFORE QUALIFYING FOR UNIVERSAL SERVICE REVENUES COMPENSATION.

1. THE PROPOSAL MISMATCHES ACTUAL HISTORICAL COST REVENUE AGAINST THEORETICAL FUTURE COSTS.

Even if a forward looking proxy cost model could be validated as an appropriate means to determine both rural and non-rural ILECs' costs, the Joint Board's recommended method for

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61 *Recommended Decision* at para. 343.

deciding what portion of the identified proxy costs should be recovered via the federal high cost mechanism would need revisions to pass logical and economic muster. Having dwelt at length[62] on why costs must be based on a futuristic, idealized "efficient" network, even if it fails to recover actually-incurred historical investment and operating costs, the Joint Board unaccountably selects a *backward-looking* revenues "benchmark" to quantify the "reasonable expectation of the revenues that a telecommunications carrier would be reasonably expected to offset its cost, as estimated in the proxy model."[63] Today's rural ILEC rates were developed to recover each ILEC's actual historical or "embedded" investments and expenses under traditional public utility regulation.[64] They are not designed to recover theoretical forward looking costs, and there is no reason to assume that the national average of revenues for access and discretionary services can "reasonably" be "expec[ted] to offset" costs "estimated" by a totally different "proxy model." Thus, there is no logical basis or economic justification for subtracting non-forward-looking actual nationwide average revenues from local, access and discretionary services from forward looking costs to quantify high cost support.

2. NATIONWIDE AVERAGE REVENUES WILL NOT ACCURATELY IDENTIFY EXPECTED NON-USF REVENUES FOR RURAL LECs.

The revenues benchmark also cannot be used for rural ILECs because the nationwide average revenues-per-line it identifies will reflect the subscriber base, traffic mix, available services, level

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62 *Id.* at paras. 270, 275-277.

63 *Id.* at para. 311.

64 Even price caps have generally been based on existing rates developed to recover actual costs. To the extent that some price cap rates have been set on some version of incremental costing or that the Joint Board means to include other non-ILECs in the nationwide revenue averages, the scheme adds the fatal flaw of "apples to oranges" comparisons to that of comparing costs and revenues that proceed from different fundamental assumptions.

of subscription to discretionary services and relative importance of different revenue sources of the large urban ILECs. Since rural ILECs account for such a small segment of the industry, large, urban ILEC data will obviously swamp the information relevant to rural LEC circumstances. The recommendation acknowledges rural differences. It states, for example, that rural telephone companies "often have low local exchange rates, but high access revenues."[65] However, the proposal would subtract a *nationwide* average reflecting urban LEC revenues from local exchange, access and discretionary services from costs the proxy model has disaggregated to identify high cost rural areas. Beyond that, the Joint Board has not taken into account the Commission's promise to complete access charge reform before the new universal service mechanisms and interconnection rules go into effect. As a result, even if rural access revenues could be derived by a nationwide average, "offsetting" a level of actual charge revenues to rural ILECs based on current Part 69 results cannot give an accurate picture of what future access revenues will be available to offset costs. Nor can it be assumed that "discretionary" services such as call waiting and caller ID are even available to a rural ILEC's customers. Counting revenues from those discretionary services as revenues the rural ILEC can "reasonably expect...[to] offset" against its proxy-determined costs could be even more misleading and unfair.

3. THE BENCHMARK METHODOLOGY IGNORES THE STATUTORY CRITERIA FOR EVALUATING RATES AND HIGH COST SUPPORT.

Finally, the revenues-benchmark-and-offset method writes the principles and standards Congress enacted for rates and high cost compensation entirely out of the Act. The fundamental problem is that the revenues methodology incorrectly treats revenues paid to a rural ILEC by both

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65 *Recommended Decision* at para. 317, n. 1011.

its end users and access customers as a surrogate for the rates the customers alone pay. It is true, as the recommendation recognizes in its earlier discussion of affordability,[66] that scope of service, different state rate structures and the need for more toll service to meet basic communication needs prevents the use of a simple nationwide average local rate benchmark to compare to costs. The Joint Board correctly recognizes this problem and acknowledges rural and urban ILEC differences today in toll and access revenues.[67] However, even if the proposed average revenue measure were consistent with the forward looking cost model and even if the total revenue flows for access, local and discretionary services in rural and urban areas could be assumed to be roughly equivalent, the revenue model would not perform the function the Joint Board expects it to perform. The problem is that the recommendation has assumed that if a rural ILEC obtains a predetermined average level of *revenues* for providing access, local and discretionary services, it follows that the ILEC's customers are only being asked to absorb the same level of costs, on average, as customers elsewhere absorb. That is not the case. The access revenues paid by interexchange carriers to a rural ILEC for local pickup and delivery of the interexchange carrier's long distance traffic are not the equivalent of the price paid by rural customers for long distance service. The payments are not even made to the same carrier. Thus, if rural customers are expected to generate the same level of revenues for a comparable package of services as the rest of the nation's end users, the average revenues model must measure the payments rural end users must make to interexchange carriers for

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66 *Id.* at para. 131.

67 In some cases it is accurate to expect that total access and local revenues are roughly commensurate in urban and rural areas because higher access revenues offset the lower local rates often applicable where the scope of service is small. However, the Joint Board seems to assume this as a general fact.

the extra long distance calling that their smaller and more remote locations require them to make. The Joint Board's benign intention to identify a fair cost-recovery burden for all customers to bear before high cost compensation is available, has fallen short of the mark.

The infirmities of the revenue benchmark plan prevent the proposal from fulfilling the statutory universal service purposes and principles. The Act requires rates that are both "just, reasonable and affordable" and "reasonably comparable" in rural and urban areas. The proposal does not put the Commission in the position to judge whether the plan will deliver rates that measure up to these standards. The Act also provides that high cost support must be "specific, predictable and sufficient" to achieve the Act's universal service purposes. Yet, the Joint Board recommendation boils down to determining high cost compensation for rural ILECs by subtracting somebody else's revenues from theoretically efficient costs -- without any way to measure whether the support will be sufficient to achieve the statutory universal service purposes.

Since it is unable to take into account the impact of its flawed benchmark on rural rates, the Joint Board cannot realize its stated intention of setting a benchmark "to minimize the probability that residential rates would increase while the new support mechanisms are being implemented." The Commission would be prudent to redesign the benchmark to implement the purposes and standards enacted by Congress. In doing that it will be necessary to look more closely at the differences in costs, rates and revenue flows between urban and rural areas.

D. USING TOTAL REVENUES OF INTERSTATE CARRIERS TO CALCULATE CONTRIBUTIONS IS LAWFUL AND REASONABLE.

The 1996 Act requires contributions to support universal service to be derived from providers of interstate services.[68] The recommendation asks whether the revenue measurement it proposes to use to calculate the universal service contributions by interstate carriers to fund the federal high cost and low income mechanisms should take into account only interstate revenues or both interstate and intrastate revenues.[69] The Joint Board proposes to use both for the school, library and rural health care provider mechanisms. It leaves the issue open for the high cost and low income mechanisms, but points out several key decisions on other issues that, in its view, turn on the way the jurisdictional source of revenues issue is decided.

In considering whether to count intrastate as well as interstate revenues in calculating carrier contributions to the federal high cost and low income mechanisms, it should not be forgotten how the size of the fund is determined. There is evidence in the recommendation of a misconception that the issue is whether to increase the size of the federal USF by drawing upon intrastate revenues.[70] However, the calculation of individual carrier contributions plays no part in sizing or evaluating the sufficiency of the fund. Under the proposal, the size of the federal USF would be calculated by deducting the benchmark revenues from each eligible carrier's proxy costs. The sum of this support for all eligible carriers would determine the total size of the fund necessary for the high cost and low income programs. The use of intrastate revenues would thus be limited to apportioning that fund among all interstate carriers in an equitable and nondiscriminatory fashion, as Section 254(d) mandates. In other words, the total fund will be the same size with or without using intrastate revenues to allocate carrier contribution.

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68 47 U.S.C. Section 254(d).

69 *Recommended Decision* at paras. 817-823.

70 *Id.* at para. 817.

1. THE COMMISSION MAY NOT BASE DECISIONS ON THE SIZE OR MEANS OF CALCULATING CONTRIBUTIONS.

Before reaching the question of including intrastate revenues, it is critical to question the lawfulness of the Joint Board's decision that whether to count intrastate revenues in allocating the share of universal service support among contributors will determine other decisions about the high cost and low income programs. The Joint Board has deferred several major determinations pending resolution of this issue, including whether to reduce the Subscriber Line Charge (SLC) and the appropriate "scope and magnitude of the proxy-based fund..."[71] This stance is problematic, regardless of the merits of the intrastate revenues question. The statute prescribes the standards for federal support levels and the resulting rates for defined universal services. These include "just, reasonable and affordable" rates, rates that are "reasonably comparable" in rural and urban areas and support that is "sufficient" and "predictable." Nowhere did Congress authorize basing Joint Board recommendations or Commission decisions on either the nature or relative amounts of individual carrier contributions or the size of the support fund. Accordingly, the recommendation to regard the means of allocating responsibility for contributions among contributing carriers as the prerequisite for any other universal service decision is not valid and should be disregarded.

2. USING TOTAL REVENUES IS SOUND POLICY AND CONSISTENT WITH STATE RIGHTS.

Having disputed the separate notions that size and sufficiency determinations can rest on whether "intrastate" revenues are counted in measuring relative carrier contributions, the RTC nevertheless supports including total revenues in the allocation of contribution responsibilities among carriers. The current USF mechanism compares total, unseparated loop costs to the national

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71 *Id.* at para. 817.

average of total, unseparated loop costs in calculating the appropriate level of high cost support. That support then is regarded as within the "interstate" jurisdiction and is funded by the federal USF. The current DEM Weighting Mechanism similarly weights total, unseparated switching costs pursuant to a formula that recognizes the higher costs typically associated with "small" switches. Again, the factor is applied in the separations process, which essentially treats the support identified by this calculation as jurisdictionally "interstate." Thus, both processes can be said to recover some high "intrastate" costs from the "interstate" support mechanisms by changes in cost classification. This is not a legal or economic problem, because any distinction between "interstate" and "intrastate" costs for plant that is used for local, state toll and interstate services is inherently arbitrary and may lawfully reflect social policy.[72]

Congress expressly employed the Joint Board process set forth in Section 410(c) of the Communications Act -- a provision developed for the jurisdictional separations process and traditionally used in implementing the universal service policy -- as the method for defining universal service and designing the support mechanisms.[73] Therefore, Congress must have at least been willing to alter existing boundaries of federal and state jurisdiction when it chose the mechanism associated with jurisdictional separations to develop a revised universal support system. The Section 410(c) jurisdictional allocation of costs is a joint process because both state and federal interests are involved. The process establishes and changes jurisdictional classifications and cannot, therefore, be argued to conflict with the reservation of state jurisdiction under Section 2(b) of the

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72 *See, MCI Telecommunications Corp. v. F.C.C.*, 675 F. 2d 408-417 (D.C. Cir. 1982).

73 47 U.S.C. Section 254(a).

Communications Act over services, rates and costs that are classified as intrastate. Indeed, the Joint Board necessarily recognizes in the recommendation that the universal service support calculus can transcend rigid jurisdictional labels. It recommends counting both interstate and intrastate revenues in allocating carrier contributions for school, library and rural health care discounts.[74]

The states should benefit from this arrangement: the definition of federally-supported universal services can be broad and a substantial share of the universal service costs will be borne nationwide, as Congress intends. In contrast, if all support and discounts arguably associated with "intrastate" services were left to the individual states for recovery, the rural states would bear the lion's share of universal service support costs, and it would be extremely difficult to satisfy the statutory purpose of "reasonably comparable" rural and urban rates and services. Moreover, looking at a carrier's total revenues in allocating both federal and state universal service funds[75] should minimize the incentives for arbitrage -- to classify traffic to incur the lower of interstate and intrastate USF contribution responsibilities.

The RTC believes that it is inappropriate to place too much weight on whether revenues used to allocate the responsibility for federal universal service support, whether for education and health costs or for high cost and low income mechanisms, might be classified as "intrastate." Traditionally, the niceties of jurisdictional cost allocations have successfully been regarded as the servant of the universal service policy, not its master.[76] That sound precedent should not be abandoned in

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[74] *Recommended Decision* at para. 817.

[75] *Id.* at para. 822.

[76] *See, MCI Telecommunications Corp. v. F.C.C.*, 675 F. 2d 408-417 (D.C. Cir. 1982).

implementing the 1996 Act.

II. THE JOINT BOARD CANNOT SUBSTITUTE ITS VIEW OF COMPETITIVE NEUTRALITY FOR THE BALANCE AMONG POLICIES STRUCK BY CONGRESS.

A. ANY ADDED PRINCIPLE OF COMPETITIVE NEUTRALITY MUST NOT UNDERMINE THE RURAL POLICIES AND UNIVERSAL SERVICE PRINCIPLES EXPRESSED IN THE ACT.

The Joint Board recommends supplementing the seven principles Congress enacted by adding a new principle of competitive neutrality.[77] It correctly states that the Act allows the Joint Board to supplement the enacted list of principles and that competition is one of the fundamental policies underlying the 1996 Act. What the Joint Board and the Commission must keep firmly in mind in applying this added principle, however, is that Congress viewed universal service and nationwide infrastructure advances as equally critical policy mandates. Indeed, even in enacting legislation to mandate competition and deregulation as national telecommunications objectives, Congress carefully codified and expanded upon the universal service mandate previously derived from Section 1 of the 1934 Act.[78]

The Joint Board recommends that universal service implementation should fairly balance "the principles enacted by Congress and the proposed Joint Board addition."[79] However, the Act's stated principles should take precedence over regulators' and additions.[80] While there is no doubt

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[77] *Recommended Decision* at para. 23.

[78] 47 U.S.C. § 151.

[79] *Recommended Decision* at para. 22.

[80] Indeed, there are grounds for arguing that the principle is not a proper addition because Congress explicitly called for competitive neutrality when it deemed that standard appropriate, as in Section 254(h)(2), for example.

that competition is a fundamental Congressional policy, the statute itself evidences the Congressional belief that competition may not always automatically serve the public interest, particularly in rural areas. For example, the Act's basic mandate to lift barriers to competition, Section 253, enacts an exception for rural telephone company service areas. There, Congress provided, the states retain additional authority to exclude entry by those unwilling to accept the obligation of area-wide service and obtain state designation as eligible telecommunications carriers. In setting the ground rules for state designation of carriers eligible for universal service support mechanisms, moreover, Congress again treated rural areas differently. In urban areas, Congress required the states to designate more than one eligible carrier. In contrast, in rural telephone company service areas, Congress specified that a state must make a public interest finding before designating more than one carrier to receive support. Congress singled out rural areas for distinct treatment to recognize rural differences yet again in enacting both the rural exemption from ILEC interconnection requirements and the availability of further discretionary modification and suspension relief.

One recurrent lesson of the legislation, thus, is that Congress understands that rural conditions require special scrutiny even where pro-competitive measures are concerned. Put another way, Congress has already balanced its policies of rural competition and universal service. The Joint Board cannot rewrite the legislative balance by demanding equal weight for a principle it proposes to graft onto the statutory list. Any principle that ignores the acute public interest concern Congress repeatedly demonstrated for rural areas simply cannot meet the test in Section 254(b)(7) that an added principle must be both "necessary and appropriate for the protection of the public interest, convenience and necessity" and "consistent with this Act."

B. "COMPETITIVE NEUTRALITY" DOES NOT MEAN DISCRIMINATING AGAINST INCUMBENTS.

In addition to this requirement for applying its "competitive neutrality" principle differently in rural areas, the Joint Board should also carefully apply the "neutrality" test it espouses. Indeed, from the ILEC perspective, "neutrality" often seems to be a code term for creating a newcomer's advantage to spur entry and enhance market penetration by CLECs. A good example of this skewed "competitive neutrality" is the proposal to base universal service contributions from carriers on gross revenues net of payments to other carriers. The effect of this provision is to saddle LECs with the heaviest competitive burden of recovering support in rates they charge their customers, both end users and other carriers. In contrast, the burden of recovering each carrier's contribution from customer rates would be "equitable" and "non-discriminatory" if total retail revenues from end users were the allocation factor. It would also avoid requiring LECs to invite bypass by recovering their contribution in large part via their access charges. The concern that using gross revenues or other measures would "double count" revenues completely misses the point. The purpose of looking at revenues is simply to *allocate* the duty to contribute to a fund already "sized" in the Joint Board's plan by deducting benchmark revenues from proxy costs. Rather than a fair and "neutral" allocation based on each carrier's relative involvement in telecommunications services, the Joint Board recommendation effectively shifts the heaviest burden for universal service to the local exchange carriers. At the same time it eases the cost and competitive burdens on interexchange carriers and, possibly, even the largest ILECs that now pay Long Term Support.

On the other hand, it would involve true double counting to include universal service support receipts in the revenues measured for allocating carrier contributions. Universal Service revenues are the result of the process and should not also be rerouted through the process as an allocation factor. Counting universal service support as revenue shifts an added support burden *back* onto the very customers in high cost areas or low income households that the support is designed to alleviate.

To achieve competitive neutrality in allocating contributions, it is essential that each carrier shoulder the burden of recovering its contribution from its end users. Payments to other carriers should not be treated any differently than any other expense in providing service to end users.

C. THE COMMISSION SHOULD NOT CREATE INCENTIVES FOR CONTRIBUTING CARRIERS TO RECOUP THEIR CONTRIBUTIONS DISPROPORTIONATELY FROM CUSTOMERS WITHOUT CHOICES TO REMAIN COMPETITIVE.

The RTC agrees that the law requires contributions from carriers, imposed on a nondiscriminatory and equitable basis.[81] However, the Act also requires "just, reasonable and affordable rates," "reasonably comparable" urban and rural rates and services, and "explicit" universal service support. These cumulative requirements give the Commission and the Joint Board both the power and the duty to make sure that contributing carriers recoup their contributions in a manner consistent with all the purposes and principles of Section 254.

To accomplish this result, the Commission should (a) structure the contributions so that they will be spread equitably over *all* end-users of *all* carriers, and (b) provide guidance in recovering costs from end users consistent with the Act. Only in this way can the mechanisms ensure that some contributing carriers will not bear contribution and cost recovery burdens that competitively disadvantage them[82] and that all end users will shoulder a fair share of the cost of nationwide

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[81] *Recommended Decision* at para. 2.

[82] *NARUC v. FCC*, 737 F. 2d 1095, 1115 (D.C. Cir. 1984).

universal service.

The Commission should assess carriers with universal service contributions on a nondiscriminatory basis, such as the ratio of their revenues from end users to the total nationwide revenues from all end users of all contributing carriers' services. It should then authorize each contributing carrier to recoup its contribution from its end users by collecting a uniform nationwide amount per access line and per subscribed line or a uniform nationwide percentage of end user bills. The uniform amount would be set to raise "sufficient" universal service support, as required by the 1996 Act, via "reasonably" comparable charges for all rural and urban end users of all telecommunications services. Standardizing the end user contributions will also ensure that the recovery by carriers is adequately "explicit" -- that is, that it will not be loaded disproportionately and without public disclosure into the rates charged to customers with the most limited competitive choices.

III. THE RTC SUPPORTS AN EFFECTIVE PROGRAM IMPLEMENTING SECTION 254(h).

A. SCHOOLS AND LIBRARIES SHOULD BE ABLE TO USE DISCOUNTS FOR ANY TELECOMMUNICATIONS SERVICE AND FOR INTERNET ACCESS.

In developing the Telecommunications Act of 1996, Congress very explicitly framed an ongoing national commitment to the policy of universal telecommunications service. Additionally, Congress established a comprehensive policy that is focused on ensuring that qualifying educational providers and libraries will have access to advanced telecommunications services.

It is a well-established fact that access to advanced telecommunications services can bring about community and economic development as well as enhanced educational opportunities for students both young and old. The small rural ILECs have been leaders in the installation of advanced telecommunications infrastructure that is of a quality that supports such economic, community and educational development.

But it has not always been easy because installing such infrastructure is an expensive proposition -- and particularly so in their high-cost markets. Indeed, the rural segment of the telecommunications industry's call for relief from such costs, particularly for those levied on the end user, was one of the contributing factors leading to the creation and implementation of this new national commitment to providing affordable access to advanced telecommunications services for educational and community development purposes.

Nevertheless, while the RTC is pleased that these issues have been elevated to the national stage, and that the federal state Joint Board has for the most part developed a workable approach to implementing this statutory commitment to the development of educational opportunities for all Americans, it does have several observations, concerns, and recommendations with regard to the proposal.

1. THE JOINT BOARD'S APPROACH IS GENERALLY SATISFACTORY.

The RTC supports the basic approach of the Joint Board to implementation of Sections 254(b)(6) and 254(h) in regard to schools and libraries, with the exception of a few issues described below. In particular, we agree with the Joint Board that schools and libraries should have flexibility to purchase whatever package of telecommunications service they choose, and that supported services are not limited to services supported by the high cost recovery rules. We also agree that Internet access should be eligible for discount. While recognizing the importance of internal connections to schools and libraries, the RTC is concerned that the program be structured in such a way that any successful legal challenges to the inclusion of internal connections does not bring down the whole program. As described in C, below, the RTC concurs with the recommendation that the pre-discount price be no greater than the lowest price charged to similarly situated non-residential customers for similar services.[83] The Joint Board correctly recognizes that for this purpose "geographic area" should mean the area in which the service provider is seeking to serve customers, and that TSLRIC or TELRIC should not be used to set the pre-discount price.

The Joint Board also correctly determined that support should be based upon a percentage discount mechanism. We agree that it is essential that the beneficiaries pay a share of the cost to promote efficiency and accountability. We also agree that the amount of the discount should be greater for schools and libraries that are economically disadvantaged and for those located in high cost areas. It is appropriate that where there are federal USF support discounts for both inter and intrastate services, the state discounts should be equal to the federal discounts.[84] Aggregation of eligible and ineligible buyers is wisely prohibited by the recommendation on the grounds that it would violate the prohibition on resale. Similarly, all resale is correctly prohibited.

The bona fide request requirements on the schools and libraries are essentially sound. However, because in several states incumbent rural telephone companies do not have service areas

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[83] This price would be a ceiling, but not a floor. The statement that "service providers desire the highest possible pre-discount price" (para. 535) is perhaps just unfortunately worded. The rural telephone company members of the RTC do not practice a pricing philosophy of "highest possible price" to schools, libraries or anyone else.

[84] Although the recommendation (para. 573) is only that intrastate discounts should be at least equal to the interstate discount, given the Joint Board's discussion of the need for the service recipient to contribute to the cost of service (e.g., para. 551) it would not appear appropriate to provide federal funding for 100% discounts of intrastate service, and that probably the discounts should be identical.

certificated by state public utility commissions, these companies would be excluded from providing service by adoption of the Ameritech proposal. Since this requirement appears to duplicate the function of requiring the administrator to post service requests on a web site, it is really unnecessary. In any event, the presumption of a competitive market is that service providers will take it upon themselves to make the availability of their services known to potential customers, without the imposition of government requirements.

Finally, the RTC concurs with the recommendation that funds be collected from all telecommunications carriers that provide interstate telecommunications services, so long as separate accounting categories are maintained by the administrator and carriers are allowed to choose between reimbursement and offset.

2. ANY CAP ON THE SUPPORT FOR SCHOOLS AND LIBRARIES MUST BE ADMINISTRATIVELY SIMPLE, FAIR AND COMPATIBLE WITH SCHOOL BUDGETING PROCESSES.

The Joint Board recommends an annual cap on support to schools and libraries of $2.25 billion, with a carryover of any unused amounts.[85] The cap is justified on the basis of the statutory requirement[86] to create a universal service mechanism that is specific, predictable and sufficient.[87] On close reflection, however, it is more likely that a cap will operate contrary to each of these requirements. Unless some method is found whereby all school and library service requests are cumulated, prioritized and allocated prior to the beginning of the year, it is apparent that a given recipient will have no practical means of determining whether the discount promised by the matrix

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[85] *Recommended Decision* at para. 556.

[86] *Id.* at para. 552.

[87] *See,* 47 U.S.C. 254(b)(5).

will actually be available and hence will not be able to determine whether its telecommunications bill will be within its budget. This problem is further complicated by the fact that different schools undoubtedly operate on different academic and fiscal years, and have varying budgeting cycles. Thus, it is likely that the availability of a specific discount will not be predictable or sufficient, [88] and schools and libraries will be unable to effectively utilize the program.[89] It is contrary to logic and common sense, to claim that a cap that limits or denies support to qualified recipients when the year's allocation is consumed has any effect but to provide *in*sufficient support.

The options available to avoid this problem all appear to have some undesirable attributes, but a solution must be quickly found if the support is to begin with the next school year. The priority system discussed in the recommendation might ameliorate some of the problems in an ongoing, mature and stable system, none of which will characterize the first year of the new program. Rather, the discussion in Paragraph 556 appears directed toward allocating any underrun of the program after the first year. On the premise that the perfect should not be the enemy of the good, one alternative would be to have the first year program limited to telecommunications services, with inside wire and Internet access phased in as more reliable information can be developed and the legal status of inside wire resolved. It should be relatively straightforward exercise to survey carriers to determine

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[88] The cap would make the fund predictable as to contributors as a group, although not to individual contributors who will not be able to predict their proportion of total revenues.

[89] The RTC has consistently opposed the caps placed upon the present USF on the grounds that they are unnecessary and counterproductive. *See*, for example, NTCA Comments at 5-13, CC Docket No. 80-286, October 6, 1993. *See also*, NTCA Comments at 1, CC Docket No. 80-286, October 18, 1995. However, the participation of a limited group of regulated carrier recipients in a well understood environment at least means that the administrator can allocate any cap overrun fairly among all participants with relative ease and minimal disruption of budget expectations.